

Washington State Auditor's Office

Audit Report

Audit Services

Report No. 58127

WHATCOM COUNTY WATER DISTRICT No. 13

Whatcom County, Washington

January 1, 1994 Through December 31, 1995

Issue Date: March 28, 1997

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WHATCOM COUNTY WATER DISTRICT NO. 13
Whatcom County, Washington
January 1, 1994 Through December 31, 1995

Background

Water District No. 13 was formed in 1974 to install a sewage treatment plant prior to the establishment of a 1,300 acre recreational area by Peaceful Valley Limited Partnership. In 1975, voters approved revenue bonds for the project of \$1.2 million, to be paid off by regular sewer assessments owed primarily by the Peaceful Valley Limited Partnership. The Peaceful Valley Limited Partnership encountered financial difficulties and was unable to pay the assessments. The partnership has since gone bankrupt. The principal on the bonds matured on May 15, 1988, and the full amount is currently delinquent. Regular payments of interest have not been made since 1984. With the district unable to meet its debt requirements, several lawsuits were filed by bondholders. On February 8, 1991, the district filed for Reorganization of Debt under Chapter 9 of the United States Bankruptcy Code.

WHATCOM COUNTY WATER DISTRICT NO. 13
Whatcom County, Washington
January 1, 1994 Through December 31, 1995

**Independent Auditor's Report On Compliance With State
Laws And Regulations**

Board of Commissioners
Whatcom County Water District No. 13
Sumas, Washington

We have audited the financial statements, as listed in the table of contents, of Whatcom County Water District No. 13, Whatcom County, Washington, as of and for the fiscal years ended December 31, 1995 and 1994, and have issued our report thereon dated November 14, 1996.

We also performed tests of compliance with state laws and regulations as required by *Revised Code of Washington* (RCW) 43.09.260. This statute requires the State Auditor to inquire as to whether the district complied with the laws and the *Constitution of the State of Washington*, its own ordinances and orders, and the requirements of the State Auditor's Office.

Compliance with these requirements is the responsibility of the district's management. Our responsibility is to make a reasonable effort to identify any instances of misfeasance, malfeasance, or nonfeasance in office on the part of any public officer or employee and to report any such instance to the management of the district and to the Attorney General. However, the objective of our audit of the financial statements was not to provide an overall opinion on compliance with these requirements. Accordingly, we do not express such an opinion.

Material instances of noncompliance are (1) failures to follow requirements or violations of prohibitions contained in statutes, regulations, contracts, or grants that cause us to conclude that the aggregation of the misstatements resulting from those failures or violations is material to the financial statements or (2) considerable failure to comply with the laws and the *Constitution of the State of Washington*, the district's ordinances and orders, and the requirements of the State Auditor's Office. The results of our tests of compliance disclosed an instance of noncompliance that may materially affect the financial statements, the effects of which have not been corrected in the district's financial statements. The material instance of noncompliance noted during our audit is disclosed in the accompanying Schedule of Findings.

We considered the instance of noncompliance in forming our opinion on whether the district's financial statements are fairly presented, in all material respects, in conformity with the prescribed basis of accounting and the statutory provisions described in paragraph two of this report. This report does not affect our report dated November 14, 1996, on those financial statements.

Except for the material instance of noncompliance disclosed in the Schedule of Findings accompanying this report, the results of our tests of compliance indicate that, with respect to the items tested, the district complied, in all material respects, with the provisions referred to in the second and third paragraphs of this report, and with respect to items not tested, nothing came to our attention that

caused us to believe that the district had not complied, in all material respects, with those provisions. However, we noted the immaterial instance of noncompliance disclosed in the Schedule of Findings accompanying this report.

This report is intended for the information of management and the board of commissioners and to meet our statutory reporting obligations. This report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

Brian Sonntag, CGFM
State Auditor

November 14, 1996

WHATCOM COUNTY WATER DISTRICT NO. 13
Whatcom County, Washington
January 1, 1994 Through December 31, 1995

Schedule Of Findings

1. The District Should Pursue Settlement Of Bondholders Suit To Satisfy Debt Requirements

Whatcom County Water District No. 13 has continued to fail to generate revenues sufficient to meet its reserve and debt service requirements. This condition has been documented as a finding in the prior audit reports.

The district's Bond Resolution No. 21, Section 4, states in part:

. . . The bond fund is hereby divided into two accounts, namely, a principal and interest account and a reserve account . . . the district hereby covenants to set aside and pay into such fund out of the gross revenues of the system, a fixed amount without regard to any fixed proportion, namely: (a) into the principal and interest account . . . an amount which . . . shall in the aggregate equal the interest to become due and payable on the bonds on the next succeeding interest payment date and on or before the first day of May 1988, an amount equal to the principal payable in May 15, 1988, on remaining outstanding bonds.

Further, the district's resolution states:

Into the reserve account, all payments of assessments received in Utility Local Improvement District's No. 1 and No. 2 during the 30-day cash prepayment period of such assessments and all remaining assessment payments or installments thereon collected until there shall be a total reserve of \$204,000 therein; provided, however, that such reserve amount at an amount not less than the next succeeding two years interest requirements for the bonds

The district has been unable to accumulate the required cash reserves or make the required bond interest and principal payments. This situation is primarily the result of the Peaceful Valley Limited Partnership's financial difficulties and their failure to pay assessments on their property. In 1988, Peaceful Valley filed for bankruptcy and Whatcom County foreclosed on a number of their properties.

As of December 31, 1995, the district was unable to (a) accumulate the total required reserve of \$204,000, (b) pay the entire bond principal of \$1.2 million due on May 15, 1988, and (c) generate sufficient cash flows make regular bond interest payments. The bond interest and principal payments are now delinquent. Several lawsuits have been filed on behalf of the bondholders and the district has filed for bankruptcy. The final decisions regarding these legal actions are unknown at this time.

We recommend the district pursue the settlement of its debt.

Auditee's Response

The district is still in Chapter 9 bankruptcy and will continue to work on resolution of its debt.

2. The District Should Avoid Making Gifts Of Public Funds

During our audit of Whatcom Water District No. 13, we noted the following exceptions:

- a. The Peaceful Valley Country Club runs a club which lies on property owned by the district. The district allows the Peaceful Valley Country Club the continued use of this property without any reimbursement for its use. In response to this issue being raised during the 1990-1991 audit, the Peaceful Valley Country Club agreed to help the district cover a portion of the settlement with the district's bondholders (see Finding 1). This settlement never occurred; therefore, the district has never received any compensation for past or present use of the property from the Peaceful Valley Country Club.
- b. The district applied a 12-month retroactive commercial rate decrease to the Peaceful Valley Country Club's account. The decrease provided Peaceful Valley Country Club with a utility rate which is two thirds of the residential utility rate. Prior to the retroactive rate decrease, the Peaceful Valley Country Club's account had been delinquent for at least four months billings.
- c. The district manager was reimbursed for a complete set of tires for his personal vehicle from district funds. The district manager's employment contract does not require reimbursement for tires for his personal vehicle. Furthermore, the district manager had already received reimbursement from the district for all work related miles driven on his personal vehicle. The district had determined the mileage reimbursement rate was sufficient to cover all costs incurred when personal vehicles are used for district business.

The *Constitution of the State of Washington*, Article VIII, Section 7, states in part:

No county, city, town or other municipal corporation shall hereafter give money, or property, or loan its money, or credit to or in aid of any individual, association, company or corporation

Revised Code of Washington (RCW) 57.08.120, Lease of Real Property, states in part:

A district may lease out real property which it owns . . . and which is not immediately necessary for its purposes . . . as the board of commissioners deems proper . . . A hearing shall be held . . . at which time any and all persons who may be interested shall have the right to appear and to be heard

RCW 57.08.130, Limitation on Leasing Real Property, states in part:

The authority granted in RCW 57.08.120 shall not be exercised by the board of water commissioners unless such property is declared by

resolution of the board of commissioners to be property for which there is a future need by the district and for the use of which provision is made in the comprehensive plan of the water system

RCW 57.08.090, Rates and Charges - Foreclosure for Delinquency, states in part:

The district may, at anytime after . . . rates and charges for water supplied and penalties are delinquent for a period of sixty days, bring suit in foreclosure by civil action . . . The court may allow, in addition to the costs and disbursements provided by statute, such an attorney's fee as it adjudges reasonable . . .

. . . In addition to the right to foreclose . . . the district may also cut off all or part of the service after charges for water supplied are delinquent for a period of sixty days.

RCW 42.24.090, Municipal corporations and political subdivisions - Reimbursement claims by officers and employees, states in part:

. . . The legislative body of any municipal corporation . . . may prescribe by ordinance or resolution the amounts to be paid officers or employees thereof as reimbursement for the use of their personal automobiles or other transportation equipment in connection with officially assigned duties . . .
. . .

By allowing the continued use of district property without compensation, implementing a retroactive rate decrease and reimbursing the manager for tires for his personal vehicle, the district provided gifts of public funds. The district appeared to be unaware of the aforementioned section of the *Constitution of the State of Washington* which prohibits gifting of public funds.

We recommend the district:

- a. Require the Peaceful Valley Country Club pay the district for all past due rent.
- b. Discontinue the practice of implementing retroactive rate decreases and require the payment of the amount credited to the Peaceful Valley Country Club's account.
- c. Require the district manager to reimburse the full amount charged to the district for the purchase of tires for his personal vehicle.

Auditee's Response

a:) The district intends to reach an agreement or resolution of the rights of the parties in the golf course properties.

b:) The district will no longer make any rates retroactive.

c:) The district commissioners did not feel that the district mileage reimbursement rate was sufficient to cover all vehicular expenses, therefore a one-time compensation for tires was approved. The district commissioners felt that the district's mileage reimbursement rate was unusually low when compared with other districts and IRS standards. We now recognize our error and will not make any further such adjustments.

Auditor's Concluding Remarks

We would like to express our appreciation to Whatcom Water District No. 13 for its written response to our preliminary draft audit report. Based upon the district's representations, it appears that the matters delineated in our report have been, or are being addressed.

We would like to take this opportunity to thank the staff of Whatcom County Water District No. 13 for their assistance and cooperation during the audit process.

WHATCOM COUNTY WATER DISTRICT NO. 13
Whatcom County, Washington
January 1, 1994 Through December 31, 1995

Status Of Prior Findings

The findings contained in the prior audit report were resolved as follows:

1. The District Should Pursue Settlement Of Bondholders Suit To Satisfy Debt Requirements

Resolution: *The district has not settled suit. See Finding 1.*

2. The District Should Retain All Necessary Records

Resolution: *District has retained records as required.*

3. A Functional Control Account Should Be Used With Utility Billings And Collections

Resolution: *District has implemented a functional control account as required.*

WHATCOM COUNTY WATER DISTRICT NO. 13
Whatcom County, Washington
January 1, 1994 Through December 31, 1995

Independent Auditor's Report On Financial Statements

Board of Commissioners
Whatcom County Water District No. 13
Sumas, Washington

We have audited the Schedule of Cash Activity and Schedule of Long-Term Debt, of the various funds of Whatcom County Water District No. 13, Whatcom County, Washington, for the fiscal years ended December 31, 1995 and 1994. These financial statements are the responsibility of the district's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1 to the financial statements, Whatcom County prepares financial statements on behalf of the district on the cash basis of accounting that demonstrates compliance with Washington State statutes and the *Budgeting, Accounting and Reporting System* (BARS) manual prescribed by the State Auditor, which is a comprehensive basis of accounting other than generally accepted accounting principles.

In our opinion, except for the effect, if any, of the matters discussed in the preceding paragraph, and except that omitted disclosures might influence a user's conclusions about the district's transactions, the accompanying financial statements present fairly the cash and investment transactions and the long-term bonded indebtedness of the funds of Whatcom County Water District No. 13 for the fiscal years ended December 31, 1995 and 1994, on the prescribed basis of accounting.

The accompanying financial statements have been prepared assuming that the district will continue as a going concern. As discussed in Note 2 to the financial statements, the district has filed for

Reorganization of Debt under Chapter 9 of the United States Bankruptcy Code. Because operation of the district could be substantially impeded if the filing is approved, substantial doubt exists as to its ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Brian Sonntag, CGFM
State Auditor

November 14, 1996